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TAGS: ECON EINV EFIN SR
SUBJECT: Serbia: January-August Macro Results - Waiting for the Global Economic Crisis to Hit

Summary

¶1. Serbian macroeconomic indicators through August of this year show the first signs of the global slowdown that is beginning to hit Serbia. Import growth slowed but continued to grow faster than exports, widening the trade deficit. Local economists warn that the deficit threatens balance of payment sustainability with inevitable reductions in foreign investment as the global economy contracts due to the financial crisis. Stojan Stamenkovic of the Economic Institute said that the global crisis could hit Serbia hard, causing a significant slowdown in GDP growth and recommended that the government reduce its 2009 budget accordingly. End Summary.

Industrial Production Growth Slows in August

¶2. Serbian industrial production dropped by 8% in August 2008 compared to the previous month, or 4.4% compared to August 2007. This slowdown reduced cumulative January-August 2008 production growth from 4.3% in July to 3.1% in August year on year (y/y). The drop was distributed across nearly all sectors, led by the fall in tobacco and food industry production. The only growth was in the chemical industry and base metals. August results are typically weak with many Serbs on vacation, but few expect September results to reverse this trend.

Retail Trade Falls in August, Still Up 6.8% Cumulatively
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¶3. August 2008 retail trade volume was lower than in July by 0.7% in real terms. However, accumulated Jan-Aug y/y retail trade volume increased in real terms by 6.8% due to the strength of Serbian economic growth early in the year. The average monthly wage reached $543 in August 2008, and was up 4.23% in real terms for the first 8 months of 2008 y/y. Household demand decreased in July and August 2008 over the same months last year in real terms by 4.7% and 3.9% respectively. This reduction was mostly due to the reduction in consumer credit and an increase in household savings. Inflation slowed down in the second half of the year and the consumer price index in September 2008 y/y reached 10.9%, mostly due to decreases in oil and food prices.

Imports Growth Slows, But Trends Remain Upward
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¶4. Serbian imports also recorded a slowdown in August, reaching $1.83 billion compared to the 2008 monthly average of $2 billion. Overall, import growth continues with a January-August 2008 value of $15.95 billion, up 40% y/y. Serbian exports grew slower than imports in the same period - at a rate of 38.6% y/y and reached $7.72 billion, thus widening trade deficit to $8.23 billion. The biggest contributors to export growth were iron and steel, road vehicles, and telecommunications devices, while the largest imports were oil and gas, and industrial machines.

Current Account Deficit Up By 66.4% y/y, BOP Negative
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¶5. Local economists, including the Economic Institute's Stamenkovic, warn that the growth in the trade deficit endangers the sustainability of Serbia's balance of payments. The current account deficit increased by 66% in January-August y/y to $6.16 billion, mostly due to growth in the trade deficit. This current account deficit has been sustainable because foreign direct investment (FDI) and international portfolio investment has been strong in recent years. From January-August 2008 Serbia ran a $132 million balance of payments deficit that had to be covered from reserves. While Serbian reserves of more than $12 billion can absorb this deficit in the short-term, it is a warning of the difficulties Serbia will face in the coming months. The deficit was largely fueled by a stark turnaround in portfolio investments which went from a net inflow of $706 million in Jan-Aug 2007 to net outflow of $100 million in Jan-Aug 2008.

Worldwide Crisis Ill-timed for Serbia

¶6. Stamenkovic warned that Serbia could suffer from the global crisis in the coming year, beyond the initial hopes of simply facing an increased cost of international capital. He expected slower GDP growth in Serbia and the 2009 budget should be cut to fit this assumption, since the slowing economy meant less revenues for the budget. He listed several areas of concern: domestic demand would slow down due to decreased loans; growth in FDI would stagnate; cross-border credits had been reduced due to decreased liquidity of parent banks; EU economic slowdown would cut Serbian export growth since the EU is the biggest export market for Serbia.

COMMENT

¶7. The August statistics provide an early indicator that Serbia will not escape the effects of the global financial crisis. The crisis hits Serbia at a particularly difficult time as the new government is seeking to deliver on election promises and continue the strong economic growth of the past three years. Local economic leaders, including the Vice Chairman of Raiffeisen Bank and the Securities Commission President, told us that the real effects of the worldwide financial crisis had not hit Serbia yet, but they soon would. They claimed that liquidity in the Serbian banking sector was not threatened due to high reserve requirements (some as high as 45%). While the Serbian government has taken prudent measures to bolster confidence in the financial sector, such as increasing deposit insurance limits from $4000 to $65,000, the Serbian economy is slowing and the macroeconomic pressures in 2009 will be significant. The Serbian government will be faced with difficult choices in the next month as they prepare the 2009 budget, with revenue growth stagnating. The government hopes to renew its engagement with the IMF in order to find a scapegoat for looming budget cuts. Clearly, Serbia will struggle in 2009 economically as the effects of reduced international investment, the slowing global economy and Serbia's long running trade deficits combine to challenge the new government's agenda of delivering a better standard of living through progress toward the EU. End Comment.

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